No. 15093.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

AUTREY BROTHERS, INC., LEWIS AUTREY, STELLA AUTREY and SLEEP E-Z MATTRESS CO., a corporation,

Appellants,

vs.

FRANK M. CHICHESTER, as Trustee in Bankruptcy for The Estate of Veraco, Inc., doing business as Airest Mattress Co., Bankrupt,

Appellee.

On Appeal From the United States District Court for the Southern District of California, Central Division.

APPELLANTS' OPENING BRIEF.

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APPELLANTS' OPENING BRIEF.

Introduction.

This is an appeal by all defendants from a judgment of the United States District Court for the Southern District of California in the sum of $86,315.62 awarded a Trustee in Bankruptcy arising out of certain alleged violations of bulk sales laws, fraudulent conveyances and exemplary damages. The amount of actual damages as found by the Trial Court was $76,315.62 and the additional award of $10,000.00 was for exemplary damages. While all of the defendants below are appellants in this proceeding, special emphasis in this brief will be placed on the positions taken by Lewis Autrey and Stella Autrey.

Jurisdiction of the Court Below and Jurisdiction in This Court.

The jurisdiction of the Court below is fixed by Section 70 of the Bankruptcy Act (11 U. S. C. A. 110).

The jurisdiction of this Court is fixed by 28 U. S. C. A. 1291 and further, by Section 24 of the Bankruptcy Act (11 U. S. C. A. 47).

Sauve v. More Investment Co., 248 Fed. 642;

Stelling v. Jones Lumber Co., 116 Fed. 261.

Statement of Facts.

In order to understand the characters in this litigation, it should be noted that the appellant Lewis B. Autrey has been referred to in the record on many occasions as Buster Autrey. Lewis B. Autrey and Buster Autrey are one and the same person. Vernon Autrey is a brother of Buster Autrey and Vernon Autrey was the moving head of Veraco, Inc., the bankrupt corporation of which appellee is the trustee in bankruptcy. There are two other Autrey brothers whose names will appear from time to time in the record although they are not active participants in the factual situation upon which this litigation is grounded: they are Floyd Autrey and Eugene Autrey. Stella Autrey is the wife of Lewis Autrey.

Upon the adjudication in bankruptcy of Verco, Inc., on August 10, 1954, Frank M. Chichester, the appellee, became trustee of said bankrupt corporation. In the course of his investigation, he ascertained that in November of 1953, Veraco, Inc., had transferred certain of its retail stores in California, Utah, Oregon and Washington to Autrey Brothers, Inc., a California corporation. It was

stipulated and established that so far as the transfers of these stores were concerned that there was no compliance with the bulk sales laws of the respective states involved. [Tr. of Rec. p. 81.]

The Pleadings.

In the complaint, upon which the judgment appealed from is grounded, it was alleged that Times-Mirror Company of Los Angeles, California, was an existing creditor of Veraco, Inc., as of the date of the alleged transfers, as well as at the date of the adjudication in bankruptcy of Veraco, Inc. The first four causes of action set forth in appellee's complaint constitute separate statements of the individual transfers made in violation of the bulk sales statutes of the respective states involved. The fifth cause of action alleged that the transfers alleged in the first four causes of action rendered Veraco, Inc., insolvent. The sixth cause of action alleged that the transfers were fraudulent in fact as well as violative of the various bulk sales statutes.

The answer of the defendants placed in issue the material allegations of the complaint.

Sometime after the filing of the original action, an amended and supplemental complaint was filed seeking exemplary damages in that it alleged that after the filing of the original complaint, there had been a further transfer of the assets in question to the appellant Sleep E-Z Mattress Co., Inc., a California corporation. The answer to the amended and supplemental complaint placed in issue the material allegations of that pleading.

The Evidence.

The evidence, without contradiction, establishes that the Times-Mirror Company, the only creditor whose claim was used by appellee to establish his position as a creditor armed with process, reveals that more was paid to Times-Mirror Company between the date of the alleged fraudulent conveyances and the date of the adjudication of Veraco, Inc., than had been owed to the Times-Mirror Company on any of its accounts as of the date of the alleged fraudulent conveyances. [Tr. of Rec. pp. 90-91.] The evidence is also without contradiction to the effect that no special application was made of the funds as they were received, but the account of Veraco, Inc., was merely credited as a running account. [Tr. of Rec. p. 96.]

Appellee then called Vernon W. Autrey as a witness. Mr. Autrey did not want to testify, but was required to do so by the Court. [Tr. of Rec. pp. 97-98.] Without laboring the point as to whether the Court had a right to require Vernon Autrey to testify against his brother, his testimony indicated that he was the president of Veraco, Inc., a California corporation, from June, 1952, to the date of bankruptcy, August 10, 1953; that Lewis Autrey was his brother and that Stella Autrey was Lewis Autrey's wife. The testimony also indicates that Autrey Brothers, Inc., was operated by Lewis Autrey and constituted a manufacturing concern of bedding and mattresses and that Veraco, Inc., was a distributing company which purchased mattresses from Autrey Brothers, Inc., and sold the same through their own retail outlets. That prior to the transfers involved, the retail outlets belonged to Verco, Inc., but were transferred at the insistence of Lewis Autrey to Autrey Brothers, Inc. The witness testified that his brother had threatened him to some extent concerning an

indebtedness from Veraco, Inc., to Autrey Brothers, Inc., and that it was based upon those threats and said alleged indebtedness that the transfers were made. The record is completely clear to the effect that at the time of the transfer of the stores that Vernon Autrey honestly believed that he was indebted to Autrey Brothers, Inc., in a sum of money and it further appears, without contradiction, that at the time of the alleged transfers that both Vernon Autrey and Lewis Autrey were represented by counsel and that no force was used, that no weapons were used and that the transfers were made by Vernon Autrey as president of Veraco, Inc., on the belief that he was indebted to Autrey Brothers, Inc., in the amount claimed. [Tr. of Rec. pp. 146-147; *cf.* p. 101.]

Lewis Autrey had not been called as a witness, nor had he been subpoenaed by appellee. During the course of the discovery process prior to trial, a partial deposition of Lewis Autrey had been taken. The deposition had never been completed nor had it ever been signed or sworn to by Lewis Autrey. The record also indicates that appellee had never taken any steps to use the process of the Court to complete the deposition and have it signed and sworn to. The appellee offered the deposition in evidence at the time of trial to which strenuous objections and motions to suppress were made which were overruled by the Court. Over the objections of appellants, the deposition was received in evidence and considered by the Court. While we do not feel that the deposition establishes actual fraud, it is obvious that the record, without the deposition, is completely devoid of evidence of actual fraud. The deposition was not printed as a part of the record, but a request was filed to send the deposition up as an exhibit and we respectfully request the Court to examine the deposition.

Summary of Argument.

We propose to argue the following points of law:

1. THAT THE TIMES-MIRROR PUBLISHING COMPANY WAS NOT AN EXISTING CREDITOR WITHIN THE MEANING OF THE DECISIONS TO ENTITLE THE TRUSTEE TO THE RELIEF HE SOUGHT;

2. THAT SUBSEQUENT CREDITORS ARE NOT PROTECTED BY A VIOLATION OF THE BULK SALES LAWS;

3. THAT THE TRIAL COURT ERRED IN RECEIVING IN EVIDENCE THE INCOMPLETE DEPOSITION OF LEWIS AUTREY;

4. THAT THERE WAS AN INSUFFICIENCY OF EVIDENCE TO ESTABLISH ACTUAL FRAUD;

5. THAT THERE IS A COMPLETE FAILURE OF EVIDENCE TO ESTABLISH ANY LIABILITY OR CULPABILITY ON THE PART OF STELLA AUTREY, WIFE OF LEWIS B. AUTREY; THE EVIDENCE MERELY INDICATES SHE WAS AN OFFICER AND DIRECTOR OF AUTREY BROTHERS, INC., BUT IS DEVOID OF INDICATING ANY EVIDENCE THAT SHE IN ANY WAY PARTICIPATED IN THE ACTS COMPLAINED OF BY APPELLEE.

ARGUMENT.

1. That the Times-Mirror Publishing Company Was Not an Existing Creditor Within the Meaning of the Decisions to Entitle the Trustee to the Relief He Sought.

For the purpose of setting aside conveyances in violation of bulk sales statutes, the trustee in bankruptcy is a creditor armed with process, but in order to obtain this position, the trustee must find a creditor who was a creditor both at the time of the alleged conveyance in violation of the bulk sales statute and at the time of debtors adjudication in bankruutcy.

Moore v. Bay, 284 U. S. 4, 76 L. Ed. 133.

Bearing in mind the law on the subject, as established in *Moore v. Bay, supra,* the record indicates that the alleged fraudulent conveyances occurred in November, 1953, and that Veraco, Inc., was adjudicated a bankrupt in August of 1954. The advertising for which the indebtedness was created was published both in the Los Angeles Times and in the Mirror, both of which publications are owned by the Times-Mirror Company. The ledger sheets of the creditor introduced in evidence, indicate that Veraco, Inc., had fully paid the amount that was due as of the date of the alleged fraudulent conveyances long prior to the date of adjudication in bankruptcy. [Tr. of Rec. pp. 87, 90, 96.] Appellee has not produced "an existing creditor" within the meaning of Section 3440 of the Civil Code of the State of California or the bulk sales statutes of the other states involved in this transaction. There is a vast

difference between setting aside a fraudulent transaction for a violation of the bulk sales statutes and setting aside a fraudulent transaction based upon actual fraud.

Kirk and White Compang v. Bieg-Hoffine Co., 6 Cal. App. 2d 188, 44 P. 2d 430;

Daniels v. Pacific Brewing and Malting Company, 86 Wash. 416, 150 Pac. 609;

Oregon Mill and Grain Company v. Hyde, 87 Ore. 163, 169 Pac. 791.

The Nature of a Running Account.

The Court will recall that the testimony was to the effect that the Times-Mirror Company treated the payments made as payments on a running account and made no special application of the funds as received. [Tr. of Rec. p. 96.] California Civil Code, Section 1479, provides that in the absence of an agreement as to the application of the payments, the payments must be applied in extinction of the obligations earliest in date.

Hollywood Wholesale Electric Company v. Baskin, Inc., 121 Cal. App. 2d 415, 263 P. 2d 665;

Standard Pipe v. Red Rock Company, 57 Cal. App. 2d 897.

It will thus be evident that the Times-Mirror Company, the creditor produced by the appellee, was not "an existing creditor" within the meaning of the bulk sales laws to invest the trustee with jurisdiction to set aside the transfers. Such a creditor must be produced to place the trustee in the position of a creditor armed with process. (*Moore v. Bay, supra.*)

2. That Subsequent Creditors Are Not Protected by a Violation of the Bulk Sales Laws.

In that appellee only offered evidence as to the Times-Mirror Company, it is only fair to state that the evidence and ledger sheets received indicate that Times-Mirror Company was a subsequent creditor, having extended credit after the alleged conveyances in violation of the bulk sales statute. It requires very little argument to demonstrate that subsequent creditors are not protected by the bulk sales statutes.

Dodd v. Ranes, 1 F. 2d 658;

Calkins v. Howard, 2 Cal. App. 233, 83 Pac. 280;

Braun v. American Laundry and Machinery Co., 56 F. 2d 197;

Apex Leasing Company v. Litke, 159 N. Y. Supp. 707, 173 App. Div. 323.

It now becomes evident that appellee has failed to make a case out under his first four causes of action, which are grounded upon a violation of the bulk sales statutes, leaving the question to be determined as to whether there was proof of actual fraud to support the judgment.

3. That the Trial Court Erred in Receiving in Evidence the Incomplete Deposition of Lewis Autrey.

At the time of trial appellee produced as a witness, the reporter before whom the deposition of Lewis B. Autrey was taken [Tr. of Rec. p. 125] and upon offering the deposition in evidence, appellants moved to suppress the deposition on all of the grounds legally available [Tr. of Rec. p. 127] and despite said objections, the Court received the deposition in evidence. [Tr. of Rec. pp. 131-132.]

The record clearly shows that the deposition was never submitted to the witness for his signature nor was the deposition certified by the officer, nor was the deposition ever filed, all of which are required by Rule 30 of the Rules of Civil Procedure.

The motion to suppress was based upon the provisions of Rule 32(d) of the Rules of Civil Procedure, in that appellants had no knowledge that any attempt would be made to use the incomplete, unfiled and uncertified instrument until it was actually produced in court, at which time, the motion to suppress was made and denied, as set forth.

It is our position that the motion should have been granted and that the Court should not have read and considered the deposition, nor received it in evidence as an exhibit.

Breese v. Tampex Sales Corp., 102 F. 2d 808.

In *Thomas v. Black,* 84 Cal. 221 at 225, 226, 23 Pac. 1037, 1038, the Court stated:

> "The testimony of the witnesses . . . was improperly admitted. . . . The testimony of the two witnesses was then taken by the shorthand reporter, but was not read over to the witnesses, or corrected or signed by them. On the trial of the case, . . . a transcript of this testimony, or what purported to be such a transcript, but not certified by the reporter or by any other person, was offered in evidence, and admitted over plaintiff's objections that it had not been read to the witnesses, nor subscribed by them, nor certified by the officer taking the depositions, as required by the code, nor certified by the reporter as a correct transcript of his notes. . . . In the case at bar the transcript admitted in evidence lacked the essential elements of a 'deposition' as defined by the

code. It was not certified or authenticated in any way whatever, and the witnesses had no opportunity to correct it. The jury before whom the case was afterward tried did not see the witnesses, . . . we can see no tenable ground upon which the document could have been admitted. . . ."

To the same effect are:

Bennett v. Superior Court, 99 Cal. App. 2d 585, 222 P. 2d 276;

Beckman v. Waters, 161 Cal. 581, 119 Pac. 922.

We do not question for a moment that had Lewis B. Autrey been placed on the witness stand at the trial of this action, that the incomplete deposition could have been used for the purposes of impeachment. It was not offered for that purpose, but was offered and received as a deposition of Lewis B. Autrey and in view of the fact that the record is completely devoid of any testimony of actual fraud, it must be assumed that the Court drew the inferences of fraud from this improperly admitted deposition and for that reason, the error of law committed by the Trial Court was both substantial and prejudicial to appellants.

4. That There Was an Insufficiency of Evidence to Establish Actual Fraud.

We have fully covered this subject in our statement of facts. Lewis B. Autrey was not brought before the Court by either party and the only evidence that the Court received from Lewis B. Autry was the improperly admitted deposition. We have requested that the same be brought up with the other exhibits and we are sure that the Court will find nothing in the improperly admitted deposition to ground a finding of actual fraud.

Likewise, in perusing the testimony of Vernon Autrey, it appeared that his intentinons are clear from his testimony. At the time the transfers were made from Veraco, Inc., Vernon Autrey was under the honest belief that he was indebted or at least that Veraco, Inc., was indebted to Autrey Brothers, Inc. [Tr. of Rec. pp. 146-147.] Despite the testimony concerning threats, fear and the like, the evidence is without conflict to the effect that both Vernon Autrey and Buster Autrey were represented by counsel of their own choosing and that no force of any kind was used to accomplish the transfers. In fact the record indicates that the transfers were made on two separate occasions and it is difficult to understand that the transfers were other than freely and voluntarily made and it is also obvious that the intent and motive of Vernon Autrey was to pay out what he believed to be a financial obligation of Veraco, Inc. [Tr. of Rec. p. 147.]

5. That There Is a Complete Failure of Evidence to Establish Any Liability or Culpability on the Part of Stella Autrey, Wife of Lewis B. Autrey; the Evidence Merely Indicates She Was an Officer and Director of Autrey Brothers, Inc., but Is Devoid of Indicating Any Evidence That She in Any Way Participated in the Acts Complained of by Appellee.

A careful examination of the entire transcript will reveal that the only evidence connecting Stella Autrey with the transactions here in question appears to be that she was an officer and director of Autrey Brothers, Inc., a corporation. Assuming, for the purpose of argument, without admitting it to be a fact, that a wrong was committed, it certainly would appear that Stella Autrey was not a participant or actor in the transaction. The record does

not show that she was present at the time the transactions complained of occurred, nor did she in any way act for or on behalf of the corporation.

Let us look at the record in this regard and it will be found in the Transcript of Record, at page 101, that the following questions were asked of Vernon Autrey and the following answers given:

> "Q. Yes, who were present at the time the transfer took place? A. Myself and attorney for myself, a Mr. Silver, and Mr. Schekman and Lewis B. Autrey and Harry Traub, and it seems like brother Floyd Autrey was there at the time." [See, also, Tr. of Rec. p. 147.]

The foregoing constitutes all of the testimony on the record establishing the participants in both allegedly fraudulent transfers.

We feel that it is a fair statement of law to assert that directors, officers and agents of a corporation are not liable for corporate acts or for acts committed by other directors, officers or agents, simply by reason of their official relationship to the corporation.

There is no question that a director, officer or agent of a corporation who commits a tort is jointly personally liable along with the corporation for such tort.

> *O'Connell v. Union Drilling and Petroleum Co.*, 121 Cal. App. 302, 8 P. 2d 867;
>
> *Thomsen v. Culver City Motors, Inc.*, 4 Cal. App. 2d 639, 41 P. 2d 597;
>
> *Mears v. Crocker First National Bank*, 84 Cal. App. 2d 637, 191 P. 2d 501.

The law is entirely clear to the effect that an officer or director who does not participate in the wrongful act and is guilty of no culpable negligence in permitting it, may not be held liable for a corporate tort simply by reason of his official relationship to the corporation.

Thomsen v. Culver City Motors, Inc., 4 Cal. App. 2d 639, 41 P. 2d 597.

The record does not indicate and in fact completely negatives any act or participation by Stella Autrey in either of the two alleged fraudulent transfers made in November, 1953. Further, it fails to indicate that she was at fault in the performance of her duties as a director or officer.

"The authorities are uniform in holding nonparticipants immune from liability . . ."

O'Connell v. Union Drilling and Petroleum Co., 121 Cal. App. 302, at 309, 8 P. 2d 867, at 870.

It was further aptly stated in *Thomsen v. Culver City Motors, Inc.,* 4 Cal. App. 2d 639, at pp. at 644 and 645; 41 P. 2d 597 at 600:

"While it is true, of course, that directors and officers of a corporation are liable equally with the corporation for its torts in which they participate, it is equally true that if they do not participate therein, and if they are guilty of no culpable negligence in allowing the commission of the wrongful acts, they are not liable."

The record in this case merely establishes that Stella Autrey was a director and officer of the corporation. This

matter was brought to the attention of the Trial Court [Tr. of Rec. p. 159] and we think, of course, that any holding as to Stella Autrey is beyond the purview of a reasonable interpretation of the statutes and decisions in such cases made and provided.

Conclusion.

It is respectfully submitted that for the reasons stated that the judgment as to all appellants should be reversed and that the costs of this appeal should be taxed against appellee.

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Attorney for Appellants.